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1996 Annual Report



DELIVERING A

VISION

Choice, Quality, Security

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Choice, Quality, Security

Letter to Shareholders

Delivering Our Vision

In 1996, we took a number of important steps toward the realization of WellPoint's expansion strategy. Foremost among the significant actions taken during the year were the completion of a major acquisition outside of California and the initiation of another, the completion of a complex recapitalization, the addition of key management to the WellPoint team, and a secondary offering that more than doubled the number of WellPoint shares held by the public.

At the same time, we were able to achieve record 1996 operating results in California by relentlessly focusing on meeting the needs of our customers and containing costs. Our proven model of innovative managed care products, developed and refined over the last decade, continues to contribute to the transformation taking place in the U.S. health care industry.

In California, we have built formidable businesses by identifying customer segments and by organizing separate business units to address and fulfill the needs of those market segments. Each of our business units has its own sales, service and product development capabilities that are dedicated solely to its own customer segment.

This strategic organizational structure has enabled us to gain a competitive edge by responding quickly and creatively to market demands with innovative health care products. As a result, our growth has been impressive. In California, our HMO, CaliforniaCare®', has grown from a start-up to more than 1.0 million members in just a decade, all through internal growth.

Our geographic expansion strategy is based on our success in California in segmenting markets and gradually transforming indemnity business into a range of managed care offerings. The acquisition of the indemnity-based group health care businesses of Massachusetts Mutual®" (MassMutual) and John Hancock®, and new business developments in Texas, Georgia and the Virginia/Washington, D.C. region in 1996, were important steps in implementing our strategy. We will continue to evaluate acquisition opportunities to strengthen our position in key regional markets which we have identified as appropriate sites for the innovative products we provide.

We have set the stage for increasing value for our shareholders, providing growth opportunities for our employees and offering cost savings and choice for our customers. We are committed to delivering our vision of putting consumers back in control of their health care and giving them choice and quality at an affordable price.

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Acquisition of MassMutual Group Health Business

In March 1996, WellPoint purchased the Life and Health Benefits Management Division of MassMutual for \$402.2 million. This acquisition added 1.0 million medical members, primarily in medium-sized employer groups of between 250 and 5,000 employees.

The MassMutual business is concentrated in five geographic regions that are desirable for our regional business development. We adopted the UNICARE brand name to cover all of our activities outside of California, forming our mid-sized UNICARE business unit around the acquired MassMutual division.

For the balance of 1996, we focused on integrating MassMutual into the WellPoint management system. In addition, we launched four new regional business units--individual, small group, senior and standard (50-250 employees)--and began selling in Texas. We are moving forward with licensing and regulatory applications in Georgia, Virginia, Maryland and the District of Columbia. We

WellPoint acquired the life and health benefits management division of Massachusetts Mutual Life Insurance Company, adding approximately 1.0 million medical members.

are building the provider network systems and other infrastructures that will allow us to begin introducing our innovative managed care products in these states in 1997.

Acquisition of John Hancock Group Health Business

In October 1996, WellPoint announced the acquisition of certain portions of the group health and related life businesses of John Hancock (which closed in early 1997) for \$86.7 million. John Hancock's 1.3 million medical members, who are concentrated in many of the same areas as our mid-size members, are mostly employed by major corporations with employees in many states. This business now forms the core of our new UNICARE "Special Accounts" (large) business unit. John Hancock has achieved a superior record of providing outstanding service to its customer base. We believe this business will benefit from our ability to add creative new product offerings.

We are committed

to delivering our vision of putting consumers back in control of their health care and giving them choice and quality at an affordable price.

The Company completed a recapitalization in which the non-profit Blue Cross of California's commercial operations were acquired by Wellpoint and resulted in the formation of two public benefit foundations, owning cash and WellPoint stock valued at more than \$3 billion.

Building Critical Mass

By purchasing the health care businesses of traditional indemnity insurance companies, such as MassMutual and John Hancock, we have gained the level of membership in key geographies which we believe will allow us to build large, cost-efficient health care provider networks in these targeted locations. These networks are required in order to offer a wide variety of health plans that mix and match the features of HMO, PPO and POS plans according to the needs of our various types of customers.

Texas is an excellent example of our strategy at work. The 74,000 Texas members acquired from MassMutual formed the basis for building proprietary networks which support our four new regional business units.

By year-end, we had enrolled more than 29,000 PPO medical members in individual and small groups. The John Hancock acquisition has added another 100,000 members, giving us more than 200,000 customers in Texas, the kind of critical mass we need for our health care business model.

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strategy is the start-up of new individual, small group and senior health care businesses in the geographic areas that we have targeted for entry.

New Regional Businesses

Integral to our expansion strategy is the start-up of new individual, small group and senior health care businesses in the geographic areas that we have targeted for entry. We believe our product offerings give us a foundation for developing lasting relationships with providers and give us a competitive advantage in attracting new customers.

Recapitalization and Conversion of Blue Cross of California

On May 20, 1996, we completed a complex recapitalization transaction that converted Blue Cross of California from a non-profit enterprise into a for-profit subsidiary of WellPoint and created a \$3 billion public benefit legacy for the people of California. With this formidable task behind us, we are concentrating our resources and energy on meeting the needs of current and future customers while increasing shareholder value.

WellPoint agreed to acquire the group health and related life businesses of John Hancock Mutual Life Insurance Company. This acquisition, completed in March 1997 added 1.3 billion new medical members.

Strong Growth in California

Our California businesses achieved strong performance in 1996. We are the leader in the state in the individual and small group market and are moving toward the leadership role in the large group market, which includes large employers, governmental bodies and unions.

These successes extended to our specialty products group as well. Our Choice Dentalsm, introduced for the first time in 1996 to our large accounts in California, provides a wide range of choice in dental care. It gives

customers an ability to select a dental version of either an HMO or PPO, and move freely between the two delivery systems.

Excluding acquisitions, we have added more than 1.0 million new medical members over the past five years. Over the same five-year period, our California HMO membership experienced a compounded annual growth rate of approximately 25%. In 1996 alone, the California HMO membership grew by approximately 20%. We achieved this growth while improving the already high-quality level of our service. Our California HMO was awarded accreditation during the year by the National Committee for Quality Assurance (NCQA), an independent non-profit organization.

Almost 15 million shares of WellPoint common stock were sold in a secondary offering by the California HealthCare Foundation, a charitable foundation established as part of WellPoint's recapitalization.

Revenue and Earnings Growth for 1996

1996 was an extraordinary year with most activities devoted to establishing a solid foundation for future growth. Nonetheless, we were able to exceed earnings expectations in a year that was very volatile for our industry.

Our 1996 earnings were achieved in the face of substantial interest expense arising from the recapitalization, costs associated with two major acquisitions and investments in new business start-ups outside of California. We achieved excellent profitability in California, despite another year of substantial price competition among health plans.

Successful Secondary Common Stock Offering

As part of the conversion of Blue Cross of California and concurrent recapitalization of WellPoint, a new public benefit foundation, California HealthCare Foundation, was created. On November 21, 1996, as a first step in a long-term process of diversifying the Foundation's assets, it sold approximately 15 million of its shares to the public in a secondary offering. This offering more than doubled the number of freely tradeable shares of WellPoint to approximately 28 million, positioning the Company to attract a wider range of institutional investors.

Investment in Management and Technology

We have made substantial investments in systems development and believe that we have one of the best integrated management information systems in our industry. This includes innovative programs such as Call Caresm and StopWatch97sm, described later in this report. Each should give us a competitive advantage in soliciting new accounts, particularly large group business.

WellPoint's investments in leading-edge technologies allow us, for example, to design innovative health care products that we believe form the foundation for delivering the value and options our customers are seeking. They also enable us to administer an entire range of health and related specialty products with sophisticated business systems. This capability helps control our administrative costs and gives us the flexibility to respond rapidly to new opportunities as they unfold.

We have invested in management as well as technology. In 1996, we recruited outstanding women and men from leadership roles in the financial and health care fields to join our management teams for both California and national operations. In addition, a group of very capable staff joined us as a result of the MassMutual and John Hancock acquisitions. We now have in place what I believe to be one of the strongest, most creative and hardest-working management teams in our industry.

Responding to Change

Our industry is in the midst of transformation. Soaring costs of Medicare and fee-for-service medical plans, consumer protests against limited access HMO plans, and demands for high-quality, affordable medical care for all people are exerting great pressure for change. At the same time, these factors are creating new opportunities for WellPoint, a company that has proven its ability to respond successfully to change.

WellPoint's California medical members grew by 27% in 1996 to 3.6 million. The acquisition of the life and health benefits management division of Massachusetts Mutual Life Insurance Company added another 900,000 customers in national markets, increasing the number of WellPoint customers to 4.5 million throughout the U.S.

Our Board is also undergoing change. This year, Robert Knight will retire after 11 years of service on the Blue Cross of California and WellPoint Boards. Personally, and on behalf of all his colleagues, I want to thank Bob for his many contributions to the success of our company.

I welcome our newest employees who have joined us from MassMutual and John Hancock. And I extend my sincere thanks to all of our valued employees and directors for their contributions to WellPoint's success and to our vision of choice, quality and security. Together we are making aggressive strategies work and delivering a vision that puts Americans back in control of

A handwritten signature in black ink, appearing to read "Leonard D. Schaeffer", with a stylized, sweeping flourish at the end.

their health and security.

Leonard D. Schaeffer
Chairman and Chief Executive Officer
March, 1997

